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In The

Supreme Court of the United States

HALL STREET ASSOCIATES, L.L.C.,

Petitioner,

v.

MATTEL, INC.

On Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit

SUPPLEMENTAL REPLY BRIEF FOR RESPONDENT

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TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

ARGUMENT 1

I. PETITIONER INVOKES NONEXISTENT LEGAL AUTHORITY AND DISREGARDS THE FEDERAL AND STATE SUBSTANTIVE LAW THAT, IN THIS CASE, PROHIBITED JUDICIAL REVIEW OF THE ARBITRATION AWARD FOR LEGAL OR FACTUAL ERROR 2

A. Petitioner Identifies No Statute Or Court Rule That Authorized The District Court's Vacatur Of The Award Under The Parties' Hybrid Scheme Of Arbitration And Judicial Review For Legal Or Factual Error 2

B. Federal Common Law Has No Role Here Because The Grounds For Vacatur Of An Arbitration Award Are Substantive Law Under Erie So If The FAA Did Not Govern, State Law Would 4

C. Petitioner's Invocation Of "Inherent Authority" Disregards The Strict Limits Accompanying That Extraordinary Authority 7

II. THE PARTIES' AGREEMENT AND THEIR COURSE OF CONDUCT BELOW REFLECT THEIR RELIANCE ONLY ON THE FAA AND NOT ON SOME OTHER UNNAMED SOURCE OF AUTHORITY 9

III. PETITIONER HAS WAIVED RELIANCE ON ANY AUTHORITY OUTSIDE THE FAA 10

CONCLUSION 12

TABLE OF AUTHORITIES

CASES:

Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995) 5

In re Atlantic Pipe Corp., 304 F.3d 135 (1st Cir. 2002) 3

Bernhardt v. Polygraphic Co., 350 U.S. 198 (1956) 6

Carlisle v. United States, 517 U.S. 416 (1996) 8

Degen v. United States, 517 U.S. 820 (1996) 7

Erie Railroad Co. v. Tompkins, 304 U.S. 64 (1938) 4, 5, 6

Frew v. Hawkins, 540 U.S. 431 (2004) 8

Gasperini v. Center for Humanities, Inc., 518 U.S. 415 (1996) 6

Heckers v. Fowler, 69 U.S. 123 (1865) 7

Keith v. Volpe, 118 F.3d 1386 (9th Cir. 1997) 8

Kyocera Corp. v. Prudential-Bache Trade Services, Inc., 341 F.3d 987 (9th Cir. 2003), *cert. dismissed*, 540 U.S. 1098 (2004) 1

LaPine Tech. Corp. v. Kyocera Corp., 130 F.3d 884 (9th Cir. 1997) 1, 9

Ex parte Peterson, 253 U.S. 300 (1920) 8

Railway Employees v. Wright, 364 U.S. 642 (1961) 8

Rueda v. Union Pacific Railroad Co., 175 P.2d 778 (Or. 1946) 4

Tejas Development Co. v. McGough Bros., 165 F.2d 276 (5th Cir. 1947) 6

STATUTES AND RULES:

Federal Arbitration Act, 9 U.S.C. § 1 *et seq.*:

§ 7 9
§ 9 ..... *passim*
§ 10 ..... 2, 11, 12
§ 11 ..... 2, 11, 12

Alternative Dispute Resolution Act of 1998, 28 U.S.C. § 651 *et seq.*:
§ 651(b) 2
§ 654 ..... 2, 3

Rules Enabling Act, 28 U.S.C. § 2072(b) 3

Judiciary Act of 1789, ch. 20, § 17, 1 Stat. 73 (1789) 7

Fed. R. Civ. P. 16 4
Fed. R. Civ. P. 16(c)(9) 3

U.S. District Court for the District of Oregon Local Rules:
Rule 16.4(e)(1)(A) 3
Rule 16.4(e)(2)(A) 3
Rule 16.4(f)(1)(D) 3
Rule 16.4(i) 3

MISCELLANEOUS:

Edward Brunet, *Replacing Folklore Arbitration with a Contract Model of Arbitration*, 74 TULANE L. REV. 39 (1999) 10

Stephen B. Burbank, *Sanctions in the Proposed Amendments to the Federal Rules of Civil Procedure,* 11 HOFSTRA L. REV. 997 (1983)..... 7

Ian R. Macneil, Richard E. Speidel & Thomas J. Stipanowich, *Federal Arbitration Law* (1994)..... 4

ARGUMENT

Petitioner's attempt to recast the arbitration agreement in this case and its provision for expanded judicial review as based on anything other than the Federal Arbitration Act (FAA) is without foundation.

The FAA was the only source of authority referenced by the parties in their arbitration agreement. The FAA was the only authority noted by the district court when it exercised the purported review for legal error at issue here and vacated the initial arbitration award, by citation to *LaPine Technology Corp. v. Kyocera Corp.*, 130 F.3d 884 (9th Cir. 1997). *LaPine* was the then-governing circuit interpretation of the FAA that allowed parties to an arbitration agreement to alter the scope of judicial review under the FAA and it did not discuss any authority other than the FAA.

Thus, petitioner is wrong in its bold assertion (Pet. Supp.Br. 1, 6) that the FAA was invoked for the first time only after the court of appeals reversed *LaPine en banc* in *Kyocera Corp. v. Prudential-Bache Trade Services*, 341 F.3d 987 (9th Cir. 2003), *cert. dismissed*, 540 U.S. 1098 (2004). Indeed, the ruling in *Kyocera* is what led *petitioner* to attempt to change course and to distinguish this case somehow from the FAA, but that was unsuccessful and short lived.

Petitioner's *certiorari* petition expressly urged that this Court reject the *en banc Kyocera* interpretation of the FAA on which the court of appeals relied, Pet. 23, and follow instead the earlier interpretation of the FAA in *LaPine* on which the district court relied, and which petitioner itself

recognized as "approv[ing] expanded judicial review *under the FAA*." Pet. 26 (emphasis added). Petitioner did not suggest that there was any source of authority other than the FAA for the judicial review it sought.

I. PETITIONER INVOKES NONEXISTENT LEGAL AUTHORITY AND DISREGARDS THE FEDERAL AND STATE SUBSTANTIVE LAW THAT, IN THIS CASE, PROHIBITED JUDICIAL REVIEW OF THE ARBITRATION AWARD FOR LEGAL OR FACTUAL ERROR

A. Petitioner Identifies No Statute Or Court Rule That Authorized The District Court's Vacatur Of The Award Under The Parties' Hybrid Scheme Of Arbitration And Judicial Review For Legal Or Factual Error

Petitioner broadly asserts (Pet. Supp.Br. 10) that the district court had "ample statutory authority" to review the arbitration award for legal error. Petitioner cites only the Alternative Dispute Resolution Act (ADRA) and the Rules Enabling Act, however, and neither of them provided such authority. And as demonstrated in our earlier brief on the merits, the FAA did not provide such authority because the grounds for refusal to confirm an award and to vacate, modify, or correct are limited to those explicitly set forth by Congress in Sections 9, 10, and 11 of the FAA.

1. The ADRA directs district courts to adopt local rules to authorize alternative dispute resolution (ADR), "except that the use of arbitration may be authorized only as provided in section 654." 28

U.S.C. § 651(b). As petitioner concedes, Section 654 provides that a district court, even with the parties' consent, "may not refer cases to arbitration when more than $150,000 is in dispute." Pet. Supp.Br. 11 n.5. Because that amount was exceeded here, the ADRA would not have permitted the adoption of a local rule authorizing judicial review of an arbitration award for legal error governing this case.

Petitioner's citation to the Rules Enabling Act disregards the fact that the statute allows a court to prescribe local rules only to the extent the rules do not "abridge, enlarge or modify any substantive right." 28 U.S.C. § 2072(b). As we demonstrate below, the grounds for review of an arbitration award are substantive and thus cannot be modified by rule.

2. The single local rule on which petitioner relies, Oregon Local Rule 16.4(e)(1)(A), did not authorize the district court in this case to vacate the arbitration award for legal error. That rule allows parties to agree to ADR, but the rule grants authority to a court only to "refer any civil case to mediation," "designate a mediator," and "stay" litigation pending ADR. *Id.* at 16.4(e)(2)(A), (f)(1)(D), (i).

Similarly, Federal Rule of Civil Procedure 16(c)(9) contemplates ADR "when authorized by statute or local rule." Those words "are a frank limitation on the district courts' authority to order [ADR] thereunder," and federal courts "must adhere to that circumscription." *In re Atlantic Pipe Corp.*, 304 F.3d 135, 142 (1st Cir. 2002).

Petitioner's repeated description of the arbitration here as "non-binding," Pet. Supp.Br. 2, 9, 11, 13, 16,

21, is an apparent attempt to invoke a reference in the Advisory Committee Note to Rule 16, to "nonbinding arbitration" as something a judge can "explore." But the parties in this case agreed to *binding* arbitration—they unequivocally (and in the language of Section 9 of the FAA) agreed that the award would be submitted to the district court for confirmation and entry of judgment. Pet. App. 15a (¶24). As petitioner earlier explained: "If no party contests the award or if the court finds neither legal error nor any statutory or common-law ground for vacatur, the award 'settles' the dispute." Pet. Reply Br. 7. The award, even if never submitted for confirmation, has binding *res judicata* effect unless vacated or modified. *Rueda v. Union Pac. R. Co.*, 175 P.2d 778, 790 (Or. 1946); 4 Ian R. Macneil, Richard E. Speidel & Thomas J. Stipanowich, *Federal Arbitration Law* § 39.6 n.4 (1994) (collecting cases from other jurisdictions).

B. Federal Common Law Has No Role Here Because The Grounds For Vacatur Of An Arbitration Award Are Substantive Law Under *Erie* So If The FAA Did Not Govern, State Law Would

Petitioner's invocation of "common law" is perplexing. Pet. Supp.Br. 14-16. It cannot be read to refer to Oregon common law because petitioner buries at the end of a footnote its single citation to an outdated Oregon decision. Whatever may have been the situation earlier, or is the situation today in other States, the Oregon statutory regime that would govern enforcement of this arbitration award—if Section 9 of the FAA did not—would not

enforce the severable provision permitting review for legal error. Resp. Supp.Br. 7-12.[1]

Instead, petitioner seeks refuge in older federal cases to argue that "ordinary" common law "principles" permit enforcement of the judicial review provision. But to say that there is no general federal common law would seem unnecessary as we approach the seventieth anniversary of *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938).

Under *Erie*, the enforcement and judicial review of arbitration awards is substantive law so that where the FAA (or the ADRA or another federal statute or rule) does not control, it is state statutes and state common law that govern the issue, not federal common law. As explained in *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 271 (1995), this Court's repeated holdings that the FAA is substantive law that must be applied by both federal and state courts when applicable, rather than

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[1] Contrary to petitioner's claim (Pet. Supp.Br. 9), respondent did not waive any opposition under Oregon law to new positions taken by petitioner. As petitioner acknowledged, it never previously attempted to rely on Oregon law in this case to justify enforcement of the judicial review provision and vacatur of the award. Oral Arg. Tr. 14:6-20. To the extent petitioner suggests (Pet. Supp.Br. 15) that respondent agreed at oral argument that the provision could be enforced under Oregon common law, it is mistaken. Respondent noted only that in circumstances where Section 9 of the FAA does not apply, state common law actions to enforce awards might be available in some States. Oral Arg. Tr. 34:23-35:1, 44:15. To the extent petitioner implies that respondent endorsed development of *federal* common law, that is contrary to counsel's statement that the application of federal common law would be "antithetical" to the FAA. *Id.* at 59:15.

procedural law applicable only in federal courts, is derived from the post-*Erie* case of *Bernhardt v. Polygraphic Co.*, 350 U.S. 198 (1956). *Bernhardt* held that if an arbitration agreement falls outside the FAA's scope (*e.g.*, it does not involve commerce), then state law governs a federal district court's decision whether the agreement is enforceable in a diversity case. *Id.* at 202-203. *Bernhardt* reasoned that "the remedy by arbitration," including the grounds for "judicial review of an award" "substantially affects the cause of action created by the State." *Id.* at 203.

Gasperini v. Center for Humanities, Inc., 518 U.S. 415 (1996), confirms that the grounds for judicial review of an arbitration award are substantive law for purposes of *Erie*. *Gasperini* held that a state law that provided a judicial standard for review of the amount of a jury's damage award applied in a federal court sitting in diversity because the State had adopted its standard to reduce the risk of excessive damage awards. *Id.* at 429-430. If federal diversity courts did not apply the state standard of review, this Court held, there would be "'substantial' variations" between the results in state and federal courts, thus violating the "twin aims" of *Erie*: "discouragement of forum-shopping and avoidance of inequitable administration of the laws." *Id.* at 428, 430.

Different standards in federal and state courts for judicial review of arbitration awards not enforced under the FAA would lead to the same problems. Arbitration "awards can become no better by going into federal court to enforce them than they would be in the State Courts." *Tejas Dev. Co. v. McGough Bros.*, 165 F.2d 276, 279 (5th Cir. 1947).

C. Petitioner's Invocation Of "Inherent Authority" Disregards The Strict Limits Accompanying That Extraordinary Authority

Petitioner erroneously suggests that apart from either state or federal law, review of an arbitration award for legal error may be based on a court's "inherent authority." Pet. Supp.Br. 12-13.

"A court's inherent power is limited by the *necessity* giving rise to its exercise." *Degen v. United States*, 517 U.S. 820, 829 (1996) (emphasis added). There is no necessity here because Congress has provided for enforcement of arbitration awards in federal court under federal and state substantive law, authorized referral of certain cases for other types of ADR, and granted other case management authority to the federal courts.

Petitioner's reliance (Pet. Supp.Br. 12-13) on *Heckers v. Fowler*, 69 U.S. 123 (1865), is misguided. Referral to arbitration and enforcement of the award in *Heckers* was not based on inherent authority but on an explicit congressional delegation of authority that is lacking in this case. *Heckers*'s recognition that federal courts "have authority to make and establish all necessary rules for the orderly conducting [of] business" was a word-for-word quotation (albeit without quotation marks) of the Judiciary Act of 1789, the then-effective statutory grant of authority to the federal courts. Stephen B. Burbank, *Sanctions in the Proposed Amendments to the Federal Rules of Civil Procedure*, 11 HOFSTRA L. REV. 997, 1004 n.30 (1983).

In addition, since Congress adopted the Rules Enabling Act to authorize the promulgation of rules of procedure, this Court has repeatedly held that federal courts lack "inherent authority" "to develop rules that *circumvent or conflict* with" those rules or with federal laws. *Carlisle v. United States*, 517 U.S. 416, 426 (1996) (emphasis added).[2] Petitioner's invocation of "inherent authority" is an attempt to do just that because it seeks to circumvent the limited grounds for judicial review of an arbitration award specified by Congress.

Petitioner's analogy to a federal court's power to enter and enforce a consent decree is also flawed. A court's "authority to adopt a consent decree comes only from the statute which the decree is intended to enforce." *Railway Employees v. Wright*, 364 U.S. 642, 651 (1961). There was no federal statute here that could have given rise to authority to vacate the arbitration award for legal error because the underlying lease dispute was a state contract action. In *Frew v. Hawkins*, 540 U.S. 431, 437 (2004), this Court made clear: "Consent decrees entered in federal court must be directed to protecting federal interests." Even where federal interests are involved, a district court may not approve a consent decree that exceeds or supplants state law except to remedy a federal law violation. *Keith v. Volpe*, 118 F.3d 1386, 1393 (9th Cir. 1997).

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[2] Likewise, in *Ex parte Peterson*, 253 U.S. 300 (1920), when the Court permitted (prior to now-governing Rule 53) the appointment of a special master to submit a report that was "essential" to the jury's function in a particular case, the Court did so only because there was no federal law or rule "which directly or by implication" forbade it. *Id.* at 312.

II. THE PARTIES' AGREEMENT AND THEIR COURSE OF CONDUCT BELOW REFLECT THEIR RELIANCE ONLY ON THE FAA AND NOT ON SOME OTHER UNNAMED SOURCE OF AUTHORITY

The FAA was not invoked for the first time on appeal as petitioner claims. Pet. Supp.Br. 1, 6. The arbitration agreement specifically cited Section 7 of the FAA; it included language that tracked the entry-of-judgment requirement of Section 9 of the FAA; and both petitioner and respondent relied on the FAA in their arguments to the district court on various points of law. Resp. Supp.Br. 18-20. Of course, the parties also referenced the agreement itself as petitioner emphasizes, Pet. Supp.Br. 5-6, 16, 18, but that is consistent with the fact that the agreement was under the FAA, and petitioner cites nothing by the parties stating otherwise.

The district court never mentioned in its orders or opinions any of the purported authority on which petitioner now seeks to rely. To the contrary, as petitioner itself explained in its *certiorari* petition, the district court approved the agreement "in reliance on the Ninth Circuit's prior holding in *LaPine*, which approved expanded judicial review *under the FAA*." Pet. 26 (emphasis added); Pet. App. 46a (district court opinion relying solely on *LaPine* as its authority to vacate the award).

Petitioner even declared unequivocally in its reply brief at the *certiorari* stage that it had "clearly contended throughout the first appeal that the expanded judicial review provision was enforceable under the FAA." Pet. Reply 3.

Petitioner now cites (Pet. Supp.Br. 2, 16) the parties' initial description of the arbitration agreement as "contract arbitration" to argue that it was not "statutory arbitration" under the FAA. But the footnote appended directly to the term "contract arbitration" cites a law review article which was the source of that phrase and which makes clear that "contract arbitration" refers to arbitration under the FAA (which the article believed could include review for legal error) and is more formal than some other arbitrations under the FAA that the article describes as "folkore arbitration." J.A. 46 n.1 (citing Edward Brunet, *Replacing Folklore Arbitration with a Contract Model of Arbitration*, 74 TULANE L. REV. 39, 65-76 (1999)). The article nowhere provides support for petitioner's attempt to move such arbitration or review outside of the FAA.

III. PETITIONER HAS WAIVED RELIANCE ON ANY AUTHORITY OUTSIDE THE FAA

Petitioner's *certiorari* petition (and the related reply brief) contains no argument that when the district court refused respondent's request to enter judgment on the award and granted petitioner's request for vacatur and modification, the court exercised any of the purported non-FAA authority that petitioner now invokes. To the contrary, the passages earlier discussed, Resp. Supp.Br. 22-23, disprove petitioner's contention in its supplemental brief.

Moreover, petitioner admits that it argued in its merits brief that it should prevail because the FAA could be interpreted to authorize parties to alter the grounds for vacatur listed in Section 10 of the FAA. Pet. Supp.Br. 8-9 n.3.

The objections raised by petitioner in its supplemental brief (Pet. Supp.Br. 17-18, 19), to the characterization in respondent's merits brief of the proceedings below as being under the FAA, ring hollow in light of petitioner's notable failure to make any such objection in its merits reply brief.

Indeed, petitioner now confuses the issue when it asserts that it, Hall Street, "never brought a 'cause of action under Section 9' to confirm the arbitration agreement." Pet. Supp.Br. 18. Well, of course it did not. The initial arbitration award was adverse to petitioner and it had no interest in a court confirming the award. It was respondent who requested that the court enter judgment on the award, J.A. 51 (¶1), under the agreement's provision that was rooted in the language of Section 9. Pet. App. 15a (¶24).

Petitioner also waived any argument for vacatur or modification of the arbitration award through any type of new court action apart from the FAA when petitioner failed to preserve its severability argument. The court of appeals ruled that the provision for judicial review of legal error was invalid under the FAA and was severable under Oregon law from the remainder of the agreement that made the award enforceable under Section 9 of the FAA. Thus, the court of appeals' order to the district court to enforce the original arbitration award in favor of respondent was appropriate because petitioner failed to establish vacatur or modification on the grounds identified in Sections 10 and 11. To the extent petitioner now invokes (erroneously in our view) authorities on which it could attempt to pursue some type of new suit to try to vacate the award, affirmation of the judgment by

this Court on FAA grounds would foreclose such an action because the federal court is bound to enter judgment on the initial award under Section 9.

Finally, in light of petitioner's argument in its supplemental briefing that the district court's vacatur of the initial arbitration award was based exclusively on something other than the FAA and not even in part on the FAA, Pet. Supp.Br. 4-5, 8, 15-16, 18, it has abandoned any argument under the FAA. Because the important federal statutory question whether parties may alter the standards enumerated by Congress in Sections 10 and 11 of the FAA is no longer pressed by petitioner, dismissal of the writ as improvidently granted in this case would be appropriate.

CONCLUSION

For the reasons set forth above and in respondent's earlier briefs, the judgment of the court of appeals should be affirmed or the writ dismissed.

Respectfully submitted,

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